



TREASURER OF THE STATE OF LOUISIANA

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FUNDING REVIEW PANEL Established by Act No. 448 (HB 682) of the 2005 Regular Session

Minutes of Meeting
Tuesday, October 18, 2005

Mr. James H. Napper II, Executive Counsel for the State Treasury and designee of the chairman, State Treasurer John Neely Kennedy, called the meeting to order at 1:02 p.m. in Committee Room 4 of the State Capitol, Baton Rouge, LA. The secretary called the role.

(1) CALL TO ORDER AND ROLL CALL

Recommendations Committee: voting members

Members Present:

Mr. James H. Napper II, Chairman
Mayor John A. Berthelot
Mr. Stacy Birdwell
Lt. Henry Dean
Mr. Sam Jones (*joined the meeting after Roll Call*)
Mr. Bob Rust

Members Absent:

Mayor Randy Roach

Advisory Committee: non-voting members

Members Present:

Mr. Charlie Fredieu
Rep. Brett Geymann
Mr. Chris Nassif

Members Absent:

Sen. Walter J. Boasso
Sen. Butch Gautreaux
Rep. Pete Schneider
Governor's appointment - unfilled

Mr. Napper appointed Rep. Geymann and Mr. Nassif to serve on the Recommendations Committee in the absence of Mayor Roach and Mr. Jones.

Staff Members Present:

Laura Gail Sullivan - Panel Attorney
Karen Stephens - Panel Secretary
Thomas N. Rice - Acting Legislative Actuary
David Mayeaux - Sergeant at Arms

Witnesses Present:

Mr. Gary Curran - Municipal Employees' Retirement System (MERS) & Firefighters' Retirement System (FRS) Actuary
Mr. Charles Hall - Municipal Police Employees' Retirement System (MPERS) Actuary

(2) REVIEW AND APPROVAL OF MINUTES

Approval of the minutes of the August 23, 2005 meeting was postponed until the next meeting.

(3) PRESENTATIONS BY STAFF AND SYSTEM ACTUARIES

(a) Benefit Structure: Who gets what, and when?

Ms. Sullivan outlined the basic components of a retirement plan benefit structure: eligibility for regular and disability benefits, regular and disability benefit formulae, and survivor benefits.

Mr. Rice distributed a hand-out (Attachment 1), a preliminary portion of the *"2004 Actuarial Report on Louisiana Public Retirement Systems - October 2005"*, prepared by the office of the Legislative Auditor. He gave a brief outline of the benefit accrual rate, retirement eligibility age and service, and members contribution for FRS, MERS Plan A and Plan B, and MPERS.

Mr. Napper asked for clarification of "actuarially reduced benefit". Mr. Rice said the reduction in benefit was determined by looking at the actuarial present value, which was different from "present value" used for other financial reasons. He said the benefit was adjusted down to account for the difference in value.

Mr. Curran said, in the case of MERS, the age at which the reduction was figured from was not the age at which the person would be entitled to a deferred retirement, but the age at which he would be entitled to retirement, had he been assumed to be in continuous service. He said the MERS retiree would receive a bit of a subsidy and not a strict actuarial reduction, as with the other systems.

Mr. Rice said it was difficult to compare benefit structures for the three systems, because of nuances such as the one Mr. Curran outlined.

Ms. Sullivan said, of the three systems to be examined, only FRS did not provide for an early retirement with actuarial reduction.

Mr. Stockstill, FRS Executive Director, gave a lengthy explanation of disability benefits. Ms. Sullivan asked how long a member must be employed before disability benefits could take effect. Mr. Stockstill said five years for a "not in the line of duty" disability and anytime for an "in the line of duty" disability. Mr. Rice said that MPERS had the same year requirements. He explained the MPERS disability benefits, and the death benefits for the three systems, and touched on the recently legislated death benefit increase from \$50,000 to \$250,000.

Mr. Nassif said, "You're talking about a benefit that has nothing to do with the retirement system ... As a police officer, I know why those provisions were put in place and ... I just don't think that should be compared for the retirement system benefits at all."

Mr. Rice said he absolutely agreed, but also stated his belief that it was relevant to take the death benefit into account when the total compensation package was considered.

Mr. Nassif said, "I think the whole point of this [panel] ... was addressing the municipalities' struggle with our systems, as well as the state's [struggle], and I just don't want that issue [death benefits] ... which has nothing to do with the state benefits or the retirement benefits ... to confuse things. That's the only point I'm trying to make Mr. Rice. I don't think we need to confuse the benefits due [to] public service employees such as firemen and policemen, and death benefits, when you are talking about retirement. It doesn't have anything to do with our retirement system."

Mr. Napper stated his belief that Mr. Nassif's point was that the extra death benefit was not a direct cost to the retirement systems. Mr. Rice agreed and completed his explanation of the death benefits of the systems.

Mr. Sam Jones joined the meeting.

Mr. Fredieu said that if a FRS member was eligible to retire, and died while on the job, the survivor would receive the same benefit that the member would have received, had the member retired. Mr. Curran agreed. He said, "After a person has attained eligibility in age to retire - if they die while in service - what occurs in these plans is that the benefit that the spouse receives is the benefit that they would have received had the member in fact retired on that date, and elected an "Option 2" benefit. It's not exactly what he earned [Mr. Fredieu], because it's got the actuarial reduction on it, but it's the maximum he could have received, had he retired on that date and chosen Option 2, which is a joint member-survivor benefit. And it depends on the age of the two persons involved, but it's going to generally wind up to be somewhere in the neighborhood of about 83%-87% ... of the accrued benefit." Mr. Rice added that was not necessarily true for state plans. Mr. Napper said Mr. Curran's information was accurate for the three systems [under discussion].

Mr. Napper asked if the younger retirement age of police and firemen was a result of the nature of the hazardous work. Mr. Rice said yes, and that the members generally came into the system at an earlier than typical age, and left at an earlier age. Mr. Nassif added, "quite frankly, you want younger policemen starting out ... and after 30 years of doing his job, you need him to retire, both mentally and physically. And if you look at raising the retirement age, which I strongly oppose,

you might want to compare the life expectancy rates [of each group]." Mr. Napper said he did not mean to imply that he recommended a later retirement age.

Mr. Birdwell stated his belief that the life expectancy of FRS members was 10-12 years less than the general public, due to the nature of the job. He offered to provide the panel with national statistics to support his view at the next meeting.

Lt. Dean said the panel should look seriously at maintaining benefits for police and firefighters because departments would not be able to retain employees with a reduced benefit package. Mr. Rust asked if younger retirees were truly retired. Mr. Dean stated his belief that many younger retirees eventually went on to other careers.

Mr. Stockstill reminded the panel members that a comprehensive study of all of the benefits of all three of the systems was the task at hand. He implored the panel to study the benefits of the surviving children. Mr. Stockstill said the children's benefits were set a long time ago, and for the most part, have not been brought up to modern standards. Mr. Napper asked Mr. Stockstill to offer specific recommendations to the panel, prior to the next meeting. Mr. Stockstill agreed to do so.

(b) Actuarial Considerations: What is actuarial soundness, and how do we know when we've achieved it?

Ms. Sullivan said, "I think Tom [Rice] really referred to this already - the idea that you have your benefit structure - and now you're going to have to figure out how you're going to fund it. When these benefits are due, is the system going to have the money to pay the benefits? ... Gary [Curran] and Charles [Hall] are going to talk about the actuarial assumptions that go into each of these systems and this is going to be a prelude to our next meeting. In November we're going to be looking at the actual evaluations for each of these systems, so as these gentlemen explain the different actuarial assumptions, next meeting you will see the assumptions in practice ... they will talk about which assumptions they think are out of kilter, and which ones they see that may change more rapidly ... than the assumptions would expect ... I'd like for the panel to know when was the last time you did a study of each of the systems to see if those assumptions need to be changed."

Mr. Curran said the assumptions could be subdivided into four major categories, and gave a lengthy explanation of each category:

(1) Assumed rate of return - an estimate of what we think the assets are going to earn, and to the extent that the estimate is on target, more stable contributions are the result. (If the estimate is above what we return, the rates will creep upward. If the estimate is below the return, we have a declining rate and unnecessarily high contributions.) He said the rate is set "as close to reality" as possible. Mr. Curran said that, nationwide, large governmental retirement plans had an assumed rate of return of 7.75% - 8%. He said the rate has shifted down for the last few years, as people became more conservative about setting the assumption rate because of estimates of reduced expectations on investments.

(2) Assumed rate of salary increases

(3) Mortality of a group

(4) Rate of retirement, DROP, disability, termination from employment

Mr. Curran said, in addition to those major categories, survivor benefits, and children's benefits were considered. He said the experience for all of the categories was examined every year and adjustments could be made mid-stream, although every five years the data is given a thorough examination.

Mr. Napper stated his belief that the system actuaries make all of the above assumptions except for the assumed rate of return assumption. Mr. Curran said that the actuary had to "sign off" on everything, and the actuary's job was to guide the board in making that decision. Mr. Napper asked for the assumed rate of return for each of the three systems. Mr. Curran said MERS was 8% and MPERS/FRS was 7%, however the actuarial committee recently adopted a rate based on a 7.5% assumption.

Mr. Hall said that he agreed with most everything that Mr. Curran said, and added that the actuarial assumptions were based on the experience of the plan, and were therefore not as "negotiable" as the benefit structure. He said that in order to achieve "actuarial soundness" a system must have the ability to identify the liabilities and fund the liabilities in a systematic method or established formula, and have a means to enforce the funding of contributions in the event of default.

Mr. Rust asked if there could be a philosophical difference in the actuarial approach to the plan that would make a "difference", or was the approach a "science", as in actuarial science. Mr. Hall said that experience studies for the systems were conducted in a similar manner, but differences show up because of the fundamental difference in the groups. He said, "Even though you could take two retirement systems that have virtually identical benefit structures, and the bottom line is you see you've got different contribution requirements, there are several factors that could cause that to happen, but one factor that may have a large contribution to that would be the experience of the plan - the actuarial assumptions involved. A case in point is that if you look at FRS and MPERS, the benefit structures are very close, but yet you've got different experience in how the members interact with those benefits, and so we consequently have different funding requirements. The other issue that we have not talked about yet ... is the methodology that we use. We are ... bound by Constitutional Amendment No. 3 that was passed in 1986, followed by Act 81 ... the significance of Act 81 was it specifically set into law what actuarial methodology the actuaries will use for a particular system that tells them what procedures they're going to use to determine the funding requirements of that retirement system ... Act 81... lists all 13 of the systems, yet all 13 of the systems aren't using the same "cost method" - they're using different cost methods, and there are reasons for [that] ... but different cost methods will yield different funding requirements. So those are all separate issues ... but the retirement systems do have in place statutes that require the experience studies to be done at a minimum of once every five years." He said that MPERS five-year review was completed at the end of the 2003 fiscal year.

c) Issues related to Hurricanes Katrina and Rita

Mr. Curran and Mr. Hall stated their belief that it was too soon to be able to tell what the effects from Hurricanes Katrina and Rita would be on the systems. Mr. Napper said the statutory duty of the panel was to make a report with recommendations to the legislature by February 15, 2006. He stated his belief that the report should be made on the "status quo", rather than taking the hurricanes into effect, particularly since Messrs. Curran and Hall believed the effect on the systems would not truly be known for one to one and one-half years. Mr. Napper said the effect on the Insurance Premium Tax Fund alone would not be known for some time.

Mr. Hall agreed and said that an attempt to interject the effects of the hurricanes into the data would result in a distorted view of MPERS. Mr. Curran agreed that there was not much to be done about the collection of quantitative information at the present time, particularly ad valorem tax information. Mr. Napper reiterated that one of the biggest problems for all parties has been the lack of reliable information.

Mr. Rice said that he believed the focus of the panel, prior to the hurricanes, was the impact of the investment performance on the contribution levels, how the levels have climbed as a result of those investment losses, and how to pay for them.

Mr. Napper said that the effects of the hurricanes would have to be dealt with in some way, but he believed such a study was not within the purview of the panel.

(4) DISCUSSION OF FUTURE MEETINGS, SCHEDULING, AND TOPICS FOR CONSIDERATION

Mr. Napper said the next meeting was scheduled for November 29, 2005, at which time funding and valuation presentations would be made.

(5) DISCUSSION OF PROPOSED RECOMMENDATIONS AND PROCEDURES FOR MAKING THEM

Mr. Napper asked the members to talk with Ms. Sullivan about any recommendations they would like to make, in order to first make sure that the proposed recommendation was not already covered by law. Mr. Fredieu distributed a copy of the recommendation made at the August 23, 2005, meeting, relative to using the excess Insurance Premium Tax Fund (IPTF) to reduce the UAL. Mr. Napper indicated that the panel would discuss Mr. Fredieu's recommendation at the next meeting.

(6) OTHER BUSINESS

There was no other business.

Mr. Napper offered a motion to adjourn the meeting, to which there was no objection. The meeting was adjourned at 3:52 p.m.

Respectfully submitted,

James H. Napper II, designee of John Neely Kennedy
Chairman

/kls

Date approved: _____